

12. PROFIT/FEE

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12.1 OVERVIEW OF PROFIT/FEE

Profit or Fee is the total dollar amount paid to a contractor for performance over and above allowable costs (*Federal Acquisition Institute's Cost Analysis Guide*). It is the contractor's reward for assuming the risks and burdens associated with that contract and can motivate the contractor to perform efficiently and effectively. This chapter discusses the purpose of profit/fee analysis, general factors that will effect the analyst's development of contract profit/fee objectives, and the use of a structured approach for determining the pre-negotiation profit/fee position.

Table 12-1 defines Profit, Fee and Risk.

Table 12-1. Common Terms and Definitions

Terms	Definitions
Profit	Represents the excess of revenue over applicable costs of performance and is associated with fixed-price type contracts.
Fee	Represents a flat charge paid as compensation for services or supplies provided and is associated with cost reimbursement contracts.
Risk	The level of uncertainty associated with specific factors regarding contract performance.

Fixed-price contracts place a maximum burden of cost risk on the contractor: profit is reduced one dollar for each dollar that the contractor spends above the anticipated contract cost. Conversely, each dollar that the contractor does not spend toward the anticipated contract cost increases profit by one dollar. Thus, in a fixed-price contract, the amount of profit the contractor earns is ultimately a function of incurred contract costs. Since contract costs are the responsibility of the contractor, the level of profit (or loss) depends on the contractor's cost performance.

Fee, which is associated with cost reimbursable contracts, may be a fixed fee dollar amount or it may vary based on incentive structures.

Labor-hour and time and material contracts represent hybrid arrangements. The term profit is associated with these hybrid arrangements, but the cost risk assumed by a contractor is low, much like that assumed under cost reimbursement contracts. Therefore, profit is evaluated like fee in structured analysis approaches applied to labor-hour contracts and time and material contracts.

Profit/fee is an important cost element because it can provide several incentives beneficial to the Government. For instance, profit/fee plays a vital

role as a stimulant for efficient contract performance and as a reward for risks assumed by the contractor.

If the contractor is not properly rewarded, the following consequences may occur:

- The contractor may incur a loss which will diminish its ability to perform satisfactorily.
- Contractors may shy away from future procurements.
- If profit/fee is too high for the risks assumed, the contractor may lose motivation to perform efficiently.

NOTE:

Profit/fee analysis provides a means of ascertaining what a reasonable and adequate profit/fee should be, and it also provides a framework for discussing profit during negotiations. Profit/fee analysis does not necessarily produce the “right” profit/fee percentage. Rather, the appropriate profit/fee percentage is the product of a negotiation that is agreeable to both sides.

When cost analysis is required, profit/fee is included as an element of analysis. Profit/fee is not analyzed when price analysis is conducted.

12.2 CONSIDERATIONS FOR PROFIT/FEE ANALYSIS

When analyzing profit/fee, the following factors should be considered:

1. **Contractor effort:** The analyst should consider the complexity of the work and the resources required to perform the contract. As the complexity of the effort increases, the risk of failure or setbacks increases. Furthermore, more coordination is required among managers at high levels as the complexity or importance of an effort increases. Profit/fee negotiation objectives should increase as each of these factors increases.
2. **Contract cost risk:** The analyst should determine the level of cost responsibility assumed by the contractor, which is driven by contract type. A firm-fixed-price contract, for example, will place the full burden of performance (within a set price constraint) directly on the contractor. Higher profit/fee is justifiable in a fixed-price contract, unless there are provisions in the contract such as an Economic Price Adjustment (EPA) clause that mitigate cost risk. Under a cost-plus-fixed-fee contract, the contractor is guaranteed a fee regardless of cost overruns. As a result, little cost risk is assumed by the contractor; therefore, the profit/fee determination should reflect the minimal risk involved.
3. **Federal socioeconomic programs:** The analyst should consider the

amount of support given by the contractor to Federal socioeconomic programs. Greater profit/fee opportunity may be provided to contractors who display unique initiatives in these programs.

- 4. Capital investments:** The analyst should consider the contractor's investment contributions to efficient and economical contract performance. The government may award higher profits/fees to contractors who provide investment in facilities that are a direct benefit to the government.
- 5. Cost-control and other past accomplishments:** The analyst should consider any previously demonstrated effectiveness in cost control or if the contractor has taken measures resulting in productivity improvements. Higher profit/fee may be awarded to those contractors demonstrating cost control.
- 6. Independent development:** The analyst should consider if the contractor provided independent development efforts relevant to the contract end item without Government assistance. Higher profits/fees may be awarded to contractors providing these efforts.

12.3 USE OF A STRUCTURED APPROACH FOR PROFIT ANALYSIS

The above factors provide a framework for the analyst to determine a pre-negotiation position for profit/fee. Structured approaches will assist in determining profit/fee prenegotiation objectives by providing discipline for ensuring that all relevant factors are considered. These approaches promote uniformity and consistency in providing profit/fee analysis.

The current Federal Aviation Administration Acquisition Management System (FAA AMS) Procurement Guidance states: "For the purposes of establishing a negotiation position the CO may use some structured method (e.g. agency mandated weighted guidelines) for determining profit/fee appropriate for the work to be performed" [FAA AMS Procurement Guidance T3.2.3A.1.h(3)]. The most commonly used structured approach is called **weighted guidelines**.

The weighted guidelines method is a common means of determining profit/fee objectives. This method provides an organized and structured approach to evaluate and weigh the factors and cost risks inherent in a contract, and is also a source of documentation to the analyst and contracting officer. Most federal agencies use the weighted guidelines method in some variation.

Weighted guidelines analysis involves the breakdown of the various risks associated with a given contract. Each factor is evaluated in terms of the

weight it carries for successful contract completion as well as its respective degree of risk.

Two weighted guidelines forms available for use are FAA Form 4220.32 and DD Form 1547. These forms are discussed below.

12.3.1 Weighted Guidelines Using FAA Form 4220.32

Completion of FAA Form 4220.32 assists the analyst in calculating a profit/fee according to:

- The risk of the contract type,
- The risk on the contractor's effort,
- The cost risk associated with the contract, and
- The amount of facilities investment employed.

When using the FAA weighted guidelines method, shown as Figure 12-1, the analyst needs to categorize the contract as a manufacturing, research and development (R&D), or a services effort. The form assumes different risks are associated with each of the latter, as demonstrated by different weighting for each of these three contract categories.

Completing FAA Form 4220.32

The analyst inserts into Part I, Contractor Effort (lines 7 through 15) under column (b), the government position for each of the elements of cost listed in column (a). Table 12-2 provides further identification of each of the cost elements and the range of risk values.

Figure 12-1. FAA Form 4220.32

WEIGHTED GUIDELINES PROFIT/FEE OBJECTIVE (See Instructions on Reverse)						
1. CONTRACTOR IDENTIFICATION	a. COMPANY NAME			b. DIVISION NAME (IF ANY)		
	c. STREET ADDRESS		d. CITY	e. STATE	f. ZIP CODE	
2. WEIGHTED GUIDELINES CATEGORY (CHECK ONE) a. <input type="checkbox"/> MANUFACTURING c. <input type="checkbox"/> SERVICES			b. <input type="checkbox"/> RESEARCH AND DEVELOPMENT		3. TYPE OF CONTRACT	
4. BASIC PROCUREMENT INSTRUMENT IDENTIFICATION NO.						5. SPECIALIST NAME
a. PURCHASING OFFICE		b. FY	c. C/S PROD/SVCS CODE	d. PR NO.		
6. WEIGHTED GUIDELINES PROFIT FACTORS						
PROFIT/FEE FACTOR OR SUBFACTOR (a)	MEASUREMENT BASE (b)	PROFIT WAGE RANGES MFG (%) R&D (%) SVCS (%) (c) (d) (e)			ASSIGNED WEIGHT (%) (f)	PROFIT/FEE DOLLARS (g)
PART I - CONTRACTOR EFFORT						
7. MATERIAL ACQUISITION		1 TO 5	1 TO 5	1 TO 5		
a. SUBCONTRACTED ITEMS		1 TO 4	1 TO 4	1 TO 4		
b. PURCHASED PARTS		1 TO 4	1 TO 4	1 TO 4		
c. OTHER MATERIAL		1 TO 4	1 TO 4	1 TO 4		
8. ENGINEERING		9 TO 15	9 TO 15			
a. DIRECT LABOR		9 TO 15	9 TO 15			
b. OVERHEAD		6 TO 9	6 TO 9			
9. MANUFACTURING		5 TO 9	5 TO 9			
a. DIRECT LABOR		5 TO 9	5 TO 9			
b. OVERHEAD		4 TO 7	4 TO 7			
10. SERVICES				5 TO 15		
a. DIRECT LABOR				5 TO 15		
b. OVERHEAD				4 TO 8		
11. OTHER COSTS						
12. GENERAL MGMT - G & A		6 TO 8	6 TO 8	6 TO 8		
13. TOTAL EFFORT						
PART II - CONTRACTOR RISK						
14. COST RISK	(Total from Col. b)	0 TO 8	0 TO 7	0 TO 4		
PART III - FACILITIES INVESTMENT						
15. CAPITAL EMPLOYED	(Line 8 of DOT F 4220.34)	16 TO 20				
16. BASIC PROFIT/FEE OBJECTIVE	(Items 13 + 14 + 15, Col. g)					
PART IV - SPECIAL FACTORS						
17. SPECIAL PROFIT/FEE OBJECTIVE						
a. PRODUCTIVITY						
b. INDEPENDENT DEVELOPMENT		1 TO 4	1 TO 4			
c. OTHER	(Total from Item 16)	-5 TO +5	-5 TO +5	-5 TO +5		
d. TOTAL SPECIAL PROFIT/FEE OBJECTIVE						
18. SUBTOTAL PROFIT/FEE OBJECTIVE	(Items 16 + 17, col. g)					
PART V - COST OF MONEY OFFSET (Applicable to Research and Development and Services Weighted Guidelines only.)						
19. LESS: FACILITIES CAPITAL COST OF MONEY						
20. TOTAL PROFIT/FEE OBJECTIVE	(Items 18-19, col. g)					

Form FAA 4220.32 (Version 1201) (EXCEL)

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Part II, Contractor risk, compensates the contractor for its risk. A contractor's risk is less under cost reimbursement type contracts than it is under fixed priced contracts. This part is calculated by using the total effort from Part I and profit weightings addressed in Table 12-2.

Part III, Facilities Investment relates to the consideration to be given in the profit/fee objective in recognition of the investment risk associated with the facilities employed by the contractor. The measurement base is taken from FAA Form 4220.34, Contractor Facilities Capital and Cost of Money, or DD Form 1861 (see Chapter 11, "Facilities Capital Cost of Money").

The profit/fee objective (line 18) is calculated by summing the products of Parts I, II and III. This objective number can be used as a recommendation in the analyst's pre-negotiation position.

Part IV, Special Factors, is used when the contractor should be recognized for investment in productivity, for independent research and development or other special factors (i.e. socioeconomic programs, performance). The productivity factor is applied when the acquisition is a follow-on manufacturing effort, actual cost data are available to establish a baseline, and changes in item configuration are not large enough to invalidate price comparability. The dollar amount inserted under the measurement base is based on the estimated cost reduction that can be attributed to productivity gains. The independent development factor should use as its measurement base the development costs that were incurred by the contractor and not recovered (directly or indirectly) by the government. The "other" category allows the analyst to provide a (-5 or +5) range to the profit base based on the contractor's participation in federal socioeconomic programs.

If the contract is for research and development or services, the Facilities Capital Cost of Money is subcontracted from the profit/fee objective in line 21. This is done because services and R&D efforts do not require the type of facilities investment that a contractor would need to be motivated to do on a manufacturing effort.

Table 12-2 Risk Considerations and Weightings For FAA Form 4220.32

Risk Category	Factors To Consider	Range Of Risk Values		
		Manuf. %	R&D %	Service %
Materials	Includes subcontracted items, purchased parts, and other material. Consider the extent of managerial and technical efforts necessary for the prime contractor to administer subcontracting and select subcontractors, including effort to break out subcontract from sole sources through the introduction of competition. Consider whether the contractor's purchasing program contributes substantially to the performance of a contract.	Subcontract 1 to 5%	Subcontract 1 to 5%	Subcontract 1 to 5%
		Parts & other material 1 to 4%	Parts & other material 1 to 4%	Parts & other material 1 to 4%
Direct Labor	Includes engineering, service, manufacturing, and other labor. Consider the comparative quality and level of the labor skills and experience. Higher values should be assigned when engineering, professional, or highly technical skills are required. The contractor's manpower resources for meeting the required skills should also be assessed.	Eng. 9 to 15%	Eng. 9 to 15%	Eng. NA
		Manuf. 5 to 9%	Manuf. 5 to 9%	Manuf. NA
		Service (support) NA	Service (support) NA	Service (support) 5 to 15%
Indirect Costs	Includes overhead, general and administrative, and other costs. Consider the nature of the costs and how they contribute to contract performance.	Eng. 6 to 9%	Eng. 6 to 9%	Eng. NA
		Manuf. 4 to 7%	Manuf. 4 to 7%	Manuf. NA
		Service (support) NA	Service (support) NA	Service (support) 4 to 8%
		Other cost NA	Other cost NA	Other cost NA

Table 12-2. Risk Considerations And Weightings For FAA Form 4220.32 (Continued)

Risk Category	Factors To Consider	Range Of Risk Values		
		Manuf. %	R&D %	Service %
Cost Risk	Consider the contract type (Firm-Fixed-Price [FFP], Fixed-Price Incentive [FPI], Cost-Plus-Incentive-Fee [CPIF], Cost-Plus-Fixed-Fee [CPFF], Time And Materials [T&M], Labor-Hour [LH], Fixed-Price-Level-Of-Effort [FPLOE], Fixed-Price-Redeterminable [FPR]); consider the degree to which risks have been transferred to subcontractor through contract type or terms & conditions; consider whether previous work on undefinitized actions reduce risks. NOTE 1: T & M and Labor-Hour contracts are evaluated as CPFF. NOTE 2: Cost risk range for nonprofit/fee organization is -1 to 0.	CPFF 0 to 0.5%	CPFF 0 to 0.5%	CPFF 0 to 0.5%
		CPIF w/cost incentive 1 to 2%	CPIF w/cost incentive 1 to 2%	CPIF w/cost incentive 1 to 2%
		CPIF w/mult. incentives 1.5 to 3%	CPIF w/mult. incentives 1.5 to 3%	CPIF w/mult. incentives 1 to 2%
		FPI w/cost incentive- 3 to 5%	FPI w/cost incentive- 2 to 4%	FPI w/cost incentive- 2 to 3%
		FPI w/mult. incentives 4 to 6%	FPI w/mult. incentives 3 to 5%	FPI w/mult. incentives 2 to 3%
		FP w/prosp. price redeterm. 4 to 6%	FP w/prosp. price redeterm. 3 to 5%	FP w/prosp. price redeterm. 2 to 3%
		FFP 6 to 8%	FFP 5 to 7%	FFP 3 to 4%
Facilities Investment	Consider the extent to which the facilities used in performing the contract are contractor owned. Consider the extent to which the facilities result in productivity improvements directly benefiting the Government.	16 to 20%	NA	NA
Productivity	Recognize investment in modern cost-reducing facilities. Applies only to follow-on manufacturing efforts. Actual cost data must be present. NOTE: The measurement base is the estimated cost reduction.	Discretion	Discretion	Discretion
Independent Development	Consider the extent to which IR&D contributes to the FAA mission.	1 to 4%	1 to 4%	NA
Other	Consider contribution towards goals of socioeconomic programs. Consider contractor's past performance.	-5 to +5%	-5 to +5%	-5 to +5%

12.3.2 Weighted Guidelines Using DD Form 1547

Unlike FAA Form 4220.32, DD Form 1547 (Figure 12-2), does not distinguish among cost categories for the purposes of giving each element an individual impact on profit/fee. Instead, all cost elements are summed into a total

cost base which is applied to the various risk factors detailed on the form. In contrast, there are four factors given consideration: performance risk, contract type risk which includes working capital considerations, facilities capital employed, and cost efficiency.

Figure 12-2. DD Form 1547

RECORD OF WEIGHTED GUIDELINES APPLICATION						REPORT CONTROL SYMBOL DD-AT&L(Q)1751		
1. REPORT NO.		2. BASIC PROCUREMENT INSTRUMENT IDENTIFICATION NO.			3. SPIIN		4. DATE OF ACTION	
		a. PURCHASING OFFICE	b. FY	c. TYPE PROC INST CODE	d. PRISN			a. YEAR b. MONTH
5. CONTRACTING OFFICE CODE				ITEM	COST CATEGORY		OBJECTIVE	
6. NAME OF CONTRACTOR				13. MATERIAL				
				14. SUBCONTRACTS				
7. DUNS NUMBER		8. FEDERAL SUPPLY CODE		15. DIRECT LABOR				
				16. INDIRECT EXPENSES				
9. DOD CLAIMANT PROGRAM		10. CONTRACT TYPE CODE		17. OTHER DIRECT CHARGES				
				18. SUBTOTAL COSTS (13 thru 17)			0.00	
11. TYPE EFFORT		12. USE CODE		19. GENERAL AND ADMINISTRATIVE				
				20. TOTAL COSTS (18 + 19)			0.00	
WEIGHTED GUIDELINES PROFIT FACTORS								
ITEM	CONTRACTOR RISK FACTORS		ASSIGNED WEIGHTING	ASSIGNED VALUE	BASE (Item 20)		PROFIT OBJECTIVE	
21.	TECHNICAL		%					
22.	MANAGEMENT/COST CONTROL		%					
23.	PERFORMANCE RISK (COMPOSITE)				0.00			
24.	CONTRACT TYPE RISK				0.00			
25.	WORKING CAPITAL	COSTS FINANCED	LENGTH FACTOR	INTEREST RATE				
				%				
CONTRACTOR FACILITIES CAPITAL EMPLOYED			ASSIGNED VALUE	AMOUNT EMPLOYED				
26.	LAND							
27.	BUILDINGS							
28.	EQUIPMENT							
29.	COST EFFICIENCY FACTOR		ASSIGNED VALUE	BASE (Item 20)				
			%	0.00				
30.	TOTAL PROFIT OBJECTIVE							0.00
NEGOTIATED SUMMARY								
				PROPOSED	OBJECTIVE		NEGOTIATED	
31.	TOTAL COSTS							
32.	FACILITIES CAPITAL COST OF MONEY (DD Form 1861)							
33.	PROFIT							
34.	TOTAL PRICE (Line 31 + 32 + 33)			0.00	0.00		0.00	
35.	MARKUP RATE (Line 32 + 33 divided by 31)			%	%		%	
CONTRACTING OFFICER APPROVAL								
36. TYPED/PRINTED NAME OF CONTRACTING OFFICER (Last, First, Middle Initial)			37. SIGNATURE OF CONTRACTING OFFICER			38. TELEPHONE NO.		39. DATE SUBMITTED (YYYYMMDD)
OPTIONAL USE								
96.			97.		98.		99.	

DD FORM 1547, JUL 2002

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Administrative data is input into item numbers 1-12. We input FAA cost positions (prenegotiation objectives) for the noted cost elements in item numbers 13-20.

Performance risk is addressed in items 21-23. There are two components of performance risk: technical and management/cost control. The technical component addresses the technical uncertainties of the effort to be acquired while management/cost control represents the degree of management necessary to ensure contract requirements are met and to reduce and control costs. The analyst must weight the two risk components according to their respective input into total performance risk and the sum of the weights must equal 100%. The analyst must then assign a value in the form of a percentage to each risk component based on specific criteria using a scale from 3-7%, with 5% being the normal value. (There is an exception to the scale related to technology innovation, which will not be addressed here. More information on this exception may be found in guidance provided in Contract Pricing Reference Guides (DOD)).

The following guidance assumes assignments remain within the scale of 3-7%.

When conditions such as the following exist on the effort being procured, assignment of a percentage above 5% for the technical component of performance risk may be indicated:

- Existence of stringent tolerance limits for manufacturing;
- Services performed to exacting standards;
- Required use of highly skilled personnel or state of the art machinery;
- Investment by the contractor in the effort reduced FAA risk;
- Accelerated delivery schedule; and/or
- Assumption of more risk by the contractor via warranty provisions.

In contrast, if the following exist, assignment of a percentage below 5% for the technical component of performance risk may be indicated:

- Relatively simple requirements;
- Mature program;
- Routine efforts;
- Non-complex technology;
- Highly skilled personnel are not required; and/or
- Follow-on or repetitive buy.

Furthermore, the following conditions may merit assignment of a factor significantly below the normal 5%:

- Routine services;
- Production of simple items; and/or
- Simple operations with FAA furnished property.

When assigning values to the Management/Cost Control component, the following support assignment values above the normal 5%:

- Contractor's value add is considerable and difficult;
- Effort requires a high degree of integration and coordination;
- Contractor has a record of good past performance; and/or
- Proven contractor record of substantial participation in Federal socioeconomic programs, fully documented and reliable cost estimates, good make or buy decisions and strong cost tracking and control.

Assignment of the maximum value of 7% for Management/Cost Control is supported by the existence of the following criteria:

- Large scale integration of the most complex nature;
- Major international activities with significant management coordination; and/or
- Critically important milestones.

Values below normal may be indicated for Management/Cost Control where:

- Mature program, many deliveries have already been made;
- Contractor adds minimal value to the item being procured;
- Efforts are routine requiring minimal supervision;
- Contractor's proposals are of poor quality and/or late;
- Contractor has a record of cost overruns and unreliable estimates;
- Contractor displays a lack of cooperation in proposal negotiation; and/or
- Contractor puts forth a minimal effort to initiate cost reduction programs.

Values significantly below normal for Management/Cost Control may be appropriate when:

- DCAA or other audit discloses unsatisfactory management and internal control systems and/or
- Effort requires unusually low degree of management involvement.

For Item 23, Performance Risk, a composite weighted average of the weights

and values assigned to Technical and Management/Cost must be input under Assigned Value. That result is multiplied by Total Costs from Line 20 to result in the Performance Risk dollar component of the fee/profit objective.

Contract Type risk is addressed on Item 24 of DD Form 1547. Here the analyst assigns a percentage associated with contract types on a scale from 0 to 6%. The normal and range values are found in Figure 12-3. The base for Contract Type is Total Costs from Item 20. The resultant fee/profit objective associated with contract type is the product of the base and the assigned value (percentage).

Figure 12-3. DD Form 1547 Contract Type Percentages

Contract Type	Normal %		Range (%)
Firm-fixed Price, no financing	5		4 to 6.
Firm-fixed Price, with performance based payments	4		2.5 to 5.5.
Firm-fixed-price, with progress payments	3		2 to 4.
Fixed-price incentive, no financing	3		2 to 4.
Fixed-price incentive, with performance-based payments	2		0.5 to 3.5.
Fixed-price with redetermination provision			
Fixed-price incentive with progress payments	1		0 to 2.
Cost-plus incentive fee	1		0 to 2.
Cost-plus fixed fee		0.5	0 to 1.
Time-and-materials (including overhaul contracts priced on time-and-materials basis)		0.5	0 to 1.
Labor-hour		0.5	0 to 1.
Firm-fixed-price, level-of-effort		0.5	0 to 1.

Fixed price contracts with redetermination provisions should be treated like fixed price incentive contracts with below normal conditions.

Above normal values related to contract types may be considered for:

- Situations with minimal cost history;
- Long term contracts without economic protection for the contractor; and/or
- When incentives or payment schedules put high risk on the contractor.

Below normal values may be appropriate when:

- Product is mature with extensive cost history;
- Contract is short term;
- Incentives or payment schedules put less risk on contractor; and/or
- Costs were incurred prior to definitization.

Item 25 on DD Form 1547, Working Capital, applies only to fixed price contracts with progress payments. Because FAA rarely uses contracts with progress payments anymore, this item will not be addressed. Information if needed on Item 25 may be found in DOD's Contract Pricing Reference Guides.

Items 26 through 28 on DD Form 1547 are associated with Contractor Facilities Capital Employed. This is where we reward the contractor for investment in government contract facilities, equipment, etc. Completion of this section of DD Form 1547 requires the completion of another form, DD Form 1861, Contract Facilities Capital Cost of Money. The values to be inserted in DD Form 1547 under Amounts Employed by Land, Buildings, and Equipment are from DD Form 1861 (refer to Chapter 11 of this Handbook for information on DD Form 1861).

Of the facilities capital employed elements, the overall fee/profit objective being computed through the use of DD Form 1547 is affected only by the Amount Employed by Equipment and its assigned value. The scale to assign to Equipment is from 10-25%, with a normal value of 17.5%. Above normal values for Equipment may be justified in the following cases:

- The government received direct and exceptional benefits from the contractor's capital investment and/or
- The contractor demonstrated it made investments in state of the art technology that reduced acquisition costs or yielded tangible benefits to the government.

Assignment of significantly above the normal value for equipment may be justified when the contractor can demonstrate its investments in equipment provide direct and measurable efficiency benefits and yield significant reductions in acquisition costs. The maximum value of 25% may be justified when the contractor demonstrates that its equipment investment benefits are substantially above normal.

Assignment of below the normal value for equipment is appropriate when contractor investments are predominantly for commercial items, or for indirect items such as furniture, offices, or corporate aircraft.

Item 29 on DD 1547 enables additional profit associated with Cost Efficiency. However, it may or may not be appropriate. The contractor must demonstrate cost reduction efforts that specifically benefit the pending award. There is no "normal" value for this factor. If it is merited, the assigned value can not exceed 4%. The assigned value is applied to the Total Cost Objective of Item/Block 20.

Item/Block 30 of DD 1547 represents the total profit/fee objective and is

the sum of the amounts computed for Performance Risk, Contract Type Risk, Working Capital, Facilities Capital Employed (Equipment) and Cost Efficiency.

DD 1547 also provides for a Negotiation Summary record in items/blocks 31-35, in which one can record the Contractor Proposed values, FAA Objectives, and the Negotiated values.

12.4 SUMMARY

Structured approaches for determining profit/fee provide a consistent format for analyzing the risk factors and for establishing objectives for negotiations associated with contracting efforts. A structured approach is also an efficient source of documentation for a contracting officer during negotiations. The Weighted Guidelines method, the most commonly used structured approach in federal contracting, has been recommended to provide guidelines for analyzing profit/fee. This method of evaluating risks inherent within a contract assigns weights to the various factors that are determinants of the risks involved with the effort. Both FAA Form 4220.32 and DD 1547 provide Contracting Officers with structured approaches to fee/profit objective development. The use of either approach is acceptable under FAA AMS.

Alternate approaches for determining profit/fee may be used if they are deemed more appropriate for determining the proper profit/fee objective.